

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF THE WEST MCCRACKEN )  
COUNTY WATER DISTRICT FOR APPROVAL OF ) CASE NO. 2010-00454  
INCREASED RATES FOR WATER SERVICE )

ORDER

On November 23, 2010, West McCracken County Water District (“West McCracken”) tendered its application requesting the Commission to approve its proposed increase in its base rates for providing water service. Because of filing deficiencies, the Commission did not accept the application for filing until December 16, 2010.<sup>1</sup> Having performed a limited financial review of West McCracken’s operations, Commission Staff has prepared the attached report that contains its findings and recommendations regarding the proposed rates.

Finding that West McCracken should be afforded the opportunity to respond to Commission Staff’s findings and recommendation, the Commission HEREBY ORDERS that:

1. West McCracken shall have 14 days from the date of this Order to file with the Commission written comments, if any, on the findings and recommendations

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<sup>1</sup> In its application, West McCracken failed to comply with certain provisions of 807 KAR 5:001. The Commission’s Executive Director notified West McCracken of this failure by letter dated December 7, 2010. West McCracken made a supplemental filing on December 16, 2010 to correct the filing deficiencies. On December 21, 2010, the Commission deemed West McCracken’s application filed as of December 16, 2010.

contained in the attached Commission Staff Report and to request a hearing or an informal conference with Commission in this matter.

2. West McCracken's failure to file with the Commission written objections to a finding or recommendation contained in the Commission Staff Report within 14 days of this Order shall be deemed as agreement with that finding or recommendation and a waiver of any right to object to that finding or recommendation.

3. If West McCracken requests a hearing in this matter, it shall specifically identify in its written request for hearing all objections to the findings and recommendations set forth in the Commission Staff Report and shall provide a brief summary of testimony that it expects to present at hearing.

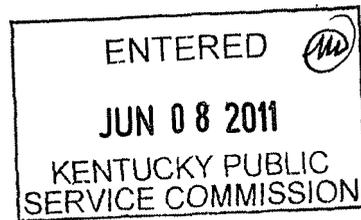
4. Within 14 days of the date of this Order, West McCracken shall file with the Commission in writing its position on adjusting its rates to the level shown in Appendix E of the Commission Staff Report.

5. If West McCracken wishes to amend its application to request the rates shown in Appendix E of the Commission Staff Report, it should request such amendment in its response to the Commission Staff Report.

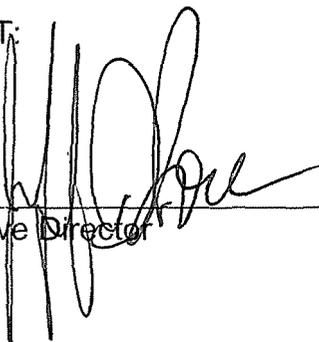
6. If West McCracken amends its application to request the rates shown in Appendix E of the Commission Staff Report, it should publish notice of its amended rate request pursuant to 807 KAR 5:011, Section 8, and shall provide the Commission with proof of publication of such notice.

7. If the Commission does not receive any written request for a hearing or for an informal conference with Commission Staff within the 14 days of the date of this Order, this case shall stand submitted to the Commission for decision based upon the existing record.

By the Commission



ATTEST:

  
\_\_\_\_\_  
Executive Director

STAFF REPORT  
ON  
WEST MCCRACKEN COUNTY WATER DISTRICT  
CASE NO. 2010-00454

West McCracken County District ("West McCracken") applied to the Commission for authority to adjust its water rates pursuant to 807 KAR 5:076. To evaluate the requested increase, Commission Staff ("Staff") performed a limited financial review of West McCracken's test period operations for the calendar year ending December 31, 2009. The scope of Staff's review was limited to obtaining information as to whether the test-period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

Mark Frost and Jason Green of the Commission's Division of Financial Analysis performed the limited review. This report summarizes Staff's review and recommendations. Mr. Green calculated the pro forma revenue adjustment and is responsible for the calculation of the rates that West McCracken could justify. Mr. Frost is responsible for all pro forma expense adjustments and the revenue requirement determination.

Appendix A to this report is West McCracken's proposed pro forma operating statement. Staff's proposed pro forma operating statement for West McCracken is shown in Appendix B. Appendix C contains an explanation of each pro forma adjustment rejected or proposed by Staff.

West McCracken’s only outstanding long-term debt issuance is a 2004 Kentucky Rural Finance Corporation (“KRWFC”) loan. Using the amortization schedule for this loan,<sup>2</sup> Staff calculates a 3-year average debt service payment of \$66,307 as shown in Table 1.

Year	Annual Debt Payments		Principal & Interest
	Principal	Interest	
2011	\$ 38,000	\$ 27,664	\$ 65,664
2012	40,000	26,347	66,347
2013	42,000	24,911	66,911
Totals	\$ 120,000	\$ 78,922	\$ 198,922
3 Year Average	\$ 40,000	\$ 26,307	\$ 66,307

West McCracken determined that its pro forma operations and a 1.2x debt service coverage (“DSC”) will support a revenue requirement from rates of \$764,954,<sup>3</sup> which is an increase of \$196,064, or 34.5 percent over normalized revenue from rates of \$568,890. However, West McCracken is limiting its request to \$57,403, which is 10.09 percent over normalized revenue from rates and will result in a revenue requirement of \$626,293.<sup>4</sup>

<sup>2</sup> Annual Report of West McCracken County Water District to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2009 at 23.

<sup>3</sup> \$787,641 (Total Revenue Requirement) - \$22,687 (Other Operating Revenue) = \$764,954.

<sup>4</sup> Application, Exhibit 4, Pro Forma, Revenue Requirement Calculation. \$568,890 (Normalized Revenue from Rates) + \$57,403 (Requested Increase) = \$626,293.

As shown in Table 2, Staff's recommended pro forma operations, annual debt service of \$66,307 and a DSC of 1.1x,<sup>5</sup> results in a revenue requirement from rates of \$760,601, which is an increase of \$191,711, or 33.7 percent over Staff's normalized revenue from rates of \$568,890.

3-Year Average Debt Service	\$	66,307
Multiplied by: Debt Service Coverage		1.10
Required Debt Service & Coverage	\$	72,938
Add: Pro Forma Operating & Maint. Exp.		496,546
Depreciation		199,277
Amortization		875
Taxes Other Than Income	+	13,722
Total Revenue Requirement	\$	783,358
Less: Other Income & Deductions	-	70
Revenue Requirement from Operations	\$	783,288
Less: Other Operating Revenues	-	22,687
Revenue Requirement from Water Sales	\$	760,601
Less: Pro Forma Revenue - Water Sales	-	568,890
Justified Increase	\$	191,711
Percentage Increase		33.7%

Staff finds that West McCracken's requested revenue requirement will produce a positive cash flow of \$72,475<sup>6</sup> and is sufficient to meet West McCracken's pro forma "cash" expenses and the debt service requirements of the KWRFC loan. Therefore,

<sup>5</sup> Because the KRWFC loan agreement does not mandate a specific DSC level, the Commission uses a 1.1x DSC.

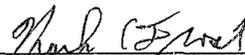
<sup>6</sup> Normalized Revenue - Water Sales	\$	568,890
Add: Requested Increase		57,403
Other & Non Operating Revenues	+	22,757
Total Revenue Requirement	\$	649,050
Less: Operating Expenses	-	710,420
Add: Depreciation & Amortization	+	200,152
Sub-total	\$	138,782
Less: Debt Service	-	66,307
Net Cash Flow	\$	72,475

Staff recommends the Commission allow West McCracken to increase its water rates to a level that will generate the requested revenue requirement of \$626,293.

In its application, West McCracken proposed to increase its rates by an across-the-board percentage applied to each rate step. It determined this percentage increase by the overall percentage increase in revenue requirement. West McCracken's present rate design is based upon cost-of-service study which the Commission reviewed in the utility's last rate adjustment proceeding.<sup>7</sup> Staff agrees that West McCracken's proposed method of an-across-the-board percentage increase to its current rates is appropriate.

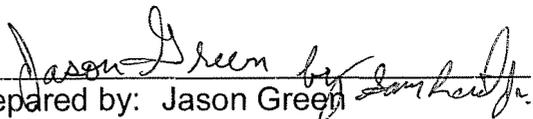
Staff recommends that the Commission approve the rates that are set forth in Appendix D. The rates contained in Appendix E will produce Staff's revenue requirement of \$760,601.

#### Signatures



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Prepared by: Mark C. Frost  
Financial Analyst, Water and Sewer  
Revenue Requirements Branch  
Division of Financial Analysis



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Prepared by: Jason Green  
Rate Analyst, Communications, Water  
and Sewer Rate Design Branch  
Division of Financial Analysis

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<sup>7</sup> Case No. 2006-00542, Application of West McCracken County Water District for Approval of a Proposed Increase in Rates for Water Service, to Increase Non-Recurring Charges, and to Revise Its Tariff Accordingly (Ky. PSC Jun. 22, 2007).

APPENDIX A  
STAFF REPORT, CASE NO. 2010-00454  
WEST MCCRACKEN'S  
PRO FORMA OPERATIONS

	Test-Period Operations	Pro Forma Adjustments	Adj. Ref	Pro Forma Operations
Operating Revenues:				
Revenues - Sales of Water	\$ 564,287	\$ 4,603	(a)	\$ 568,890
Other Operating Revenues	22,687	0		22,687
Total Operating Rev.	<u>\$ 586,974</u>	<u>\$ 4,603</u>		<u>\$ 591,577</u>
Operating Expenses:				
Operation & Maintenance:				
Salaries & Wages - Emp.	\$ 173,076	\$ (5,025)	(b)	\$ 168,051
Salaries & Wages - Officers	1,650	0		1,650
Employee Pension & Benefits	25,279	0		25,279
Purchased Water	184,289	0		184,289
Purchased Power	7,635	0		7,635
Chemicals	724	0		724
Materials & Supplies	20,069	0		20,069
Cont. Services - Accounting	8,250	0		8,250
Cont. Services - Legal	45	0		45
Cont. Services - Testing	3,913	0		3,913
Transportation	10,839	0		10,839
Ins. - Gen. Liability	9,270	0		9,270
Ins. - Worker's Compensation	4,672	0		4,672
Ins. - Other	25,440	0		25,440
Advertising	507	0		507
Bad Debt Expense	3,611	0		3,611
Miscellaneous	18,445	0		18,445
Total Operation & Maint.	<u>\$ 497,714</u>	<u>\$ (5,025)</u>		<u>\$ 492,689</u>
Depreciation	199,159	1,064	(f)	200,223
Amortization	0	875	(g)	875
Taxes Other Than Income:				
Payroll Taxes	13,209	0		13,209
Other Taxes and Licenses	1,077	0		1,077
Utility Operating Expenses	<u>\$ 711,159</u>	<u>\$ (3,086)</u>		<u>\$ 708,073</u>
Utility Operating Income	<u>\$ (124,185)</u>	<u>\$ 7,689</u>		<u>\$ (116,496)</u>
Gains/(Losses) Disp. Utility Prop.	(1,883)	1,883	(i)	0
Net Operating Income	<u>\$ (126,068)</u>	<u>\$ 9,572</u>		<u>\$ (116,496)</u>
Other Income & Deductions:				
Interest Income	70	0		70
Net Inc. Available for Debt Service	<u><u>\$ (125,998)</u></u>	<u><u>\$ 9,572</u></u>		<u><u>\$ (116,426)</u></u>

APPENDIX B  
STAFF REPORT, CASE NO. 2010-00454  
COMMISSION STAFF'S  
PRO FORMA OPERATIONS

	<u>Test-Period Operations</u>	<u>Pro Forma Adjustments</u>	Adj. Ref	<u>Pro Forma Operations</u>
Operating Revenues:				
Revenues - Sales of Water	\$ 564,287	\$ 4,603	(a)	\$ 568,890
Other Operating Revenues	22,687	0		22,687
Total Operating Rev.	<u>\$ 586,974</u>	<u>\$ 4,603</u>		<u>\$ 591,577</u>
Operating Expenses:				
Operation & Maintenance:				
Salaries & Wages - Emp.	\$ 173,076	\$ (7,371)	(b)	\$ 165,705
Salaries & Wages - Officers	1,650	0		1,650
Employee Pension & Benefits	25,279	31,497	(c)	56,776
Purchased Water	184,289	0		184,289
Purchased Power	7,635	0		7,635
Chemicals	724	0		724
Materials & Supplies	20,069	0		20,069
Cont. Services - Accounting	8,250	0		8,250
Cont. Services - Legal	45	0		45
Cont. Services - Testing	3,913	0		3,913
Transportation	10,839	0		10,839
Ins. - Gen. Liability	9,270	0		9,270
Ins. - Worker's Compensation	4,672	(335)	(d)	4,337
Ins. - Other	25,440	(24,959)	(e)	481
Advertising	507	0		507
Bad Debt Expense	3,611	0		3,611
Miscellaneous	18,445	0		18,445
Total Operation & Maint.	<u>\$ 497,714</u>	<u>\$ (1,168)</u>		<u>\$ 496,546</u>
Depreciation	199,159	118	(f)	199,277
Amortization	0	875	(g)	875
Taxes Other Than Income:				
Payroll Taxes	13,209	(564)	(h)	12,645
Other Taxes and Licenses	1,077	0		1,077
Utility Operating Expenses	<u>\$ 711,159</u>	<u>\$ (739)</u>		<u>\$ 710,420</u>
Utility Operating Income	<u>\$ (124,185)</u>	<u>\$ 5,342</u>		<u>\$ (118,843)</u>
Gains/(Losses) Disp. Utility Prop.	(1,883)	1,883	(i)	0
Net Operating Income	<u>\$ (126,068)</u>	<u>\$ 7,225</u>		<u>\$ (118,843)</u>
Other Income & Deductions:				
Interest Income	70	0		70
Net Inc. Available for Debt Service	<u><u>\$ (125,998)</u></u>	<u><u>\$ 7,225</u></u>		<u><u>\$ (118,773)</u></u>

APPENDIX C  
 STAFF REPORT, CASE NO. 2010-00454  
 COMMISSION STAFF'S RECOMMENDED  
 PRO FORMA ADJUSTMENTS

a. Metered Water Sales. West McCracken is proposing to increase its test-period revenue from metered water sales of \$564,287 by \$4,603 to a pro forma level of \$568,890. To support its proposed adjustment, West McCracken provided a test-period billing analysis.<sup>8</sup> Staff has reviewed this billing analysis, considers the analysis to be accurate and correct, and recommends that the Commission accept the proposed adjustment.

b. Salaries and Wages – Employee. West McCracken proposes to decrease its test-period salaries and wages - employee expense of \$173,076 by \$5,025 to reflect changes in West McCracken's staff.<sup>9</sup> Using the current staff level and the 2011 employee salaries, Staff calculates a pro forma salaries and wages - employee expense of \$165,705, as shown in Table 3. Accordingly, Staff proposes to decrease salaries and wages - employee expense by \$7,371.

TITLE	DATE HIRED	Salaries		
		2009	2010	2011
Customer Accounts	Jun-87	\$ 30,950	\$ 29,950	\$ 30,780
Assistant Superintendent	Jan-85	\$ 39,900	\$ 38,650	39,620
Operator	Jan-10	N/A	\$ 25,000	26,650
Superintendent	Jan-94	\$ 66,950	\$ 65,200	66,705
Part-Time Operator	Jan-10	N/A	\$ 2,100	1,950
<b>Total</b>				<b>\$ 165,705</b>

<sup>8</sup> Application, Exhibit 4, Pro Forma, Reference Notes, Adjustment A, Revenues.

<sup>9</sup> Id., Adjustment B, Employee Salaries and Wages.

c. Employee Pensions and Benefits. West McCracken reports a test-period level of employee pensions and benefits expense of \$25,279. By letter dated November 18, 2010, West McCracken was informed that the County Employees Retirement System (“CERS”) employer contribution rate would increase on July 1, 2011 to 18.96 percent. Using the current employee health insurance premiums and the July 1, 2011 CERS contribution rate, Staff calculates a pro forma level of employee pensions and benefits expense of \$56,776 as shown in Table 4. Staff proposes to increase employee pensions and benefits expense by \$31,497.

Emp. Position	Emp. Benefits		CERS	Totals
	Monthly	Annual		
Customer Accounts	\$ 565	\$ 6,780	\$ 5,836	\$ 12,616
Assistant Sup.	555	6,660	7,512	14,172
Operator	459	5,508	5,053	10,561
Superintendent	565	6,780	12,647	19,427
<b>TOTALS</b>	<b>\$ 2,144</b>	<b>\$ 25,728</b>	<b>\$ 31,048</b>	<b>\$ 56,776</b>

d. Insurance – Workers Compensation. West McCracken reports a test-period level of insurance – workers compensation expense of \$4,672. Using the current workers compensation premiums and the decreased payroll, Staff calculates a pro forma workers compensation premium of \$4,337 as shown in Table 5. Staff proposes to decrease insurance – workers compensation expense by \$335.

Classification	Payroll	Rate	Premium
Waterworks Operation & Drivers	\$ 95,305	\$ 4.21	\$ 4,012
Clerical Office Employees	\$ 70,400	\$ 0.24	169
Total Manual Premium			\$ 4,181
Increased Emp. Liability/ IEL Minimum			+ 150
Discount	\$ 4,331	x 10%	- 433
Expense Constant/ Terrorism/ Catastrophe Charge			+ 174
Special Fund Assessment	\$ 4,072	x 6.50%	+ 265
Total Premium			\$ 4,337

e. Insurance – Other. West McCracken reports a test-period level of insurance – other expense of \$25,440. Upon its review of the general ledger, Staff found that West McCracken incorrectly recorded employee health insurance premiums of \$24,959 in this expense account. To correct the misclassification, Staff proposes to decrease insurance – other expense by \$24,959.

f. Depreciation. West McCracken proposes to increase its test-period depreciation expense of \$199,159 by \$1,064 to reflect 12 months of depreciation for utility plant placed in service in 2009.<sup>10</sup> As shown in Table 6, Staff proposes to increase depreciation expense by \$118 to reflect inclusion of West McCracken’s proposed adjustment and to remove depreciation for plant that will be fully depreciated in 2011.

(1) West McCracken’s Proposed Adjustment	\$ 1,064
(2) Fully-depreciated UPIS:	
Jumbo Desk Chair	(15)
Flat File	(68)
Leather Chair	(13)
Utility Shelves	(33)
Cash Drawer	(6)
Chair - Diamond Plus	(6)
Phone/Answering Machine	(7)
Desk & Supplies	(12)
Chairs for Lobby	(57)
Tables for Lobby	(19)
Refrigerator	(44)
Laptop & Jump Drive	(117)
ARCGIS Software	(144)
New AC & Heat System	(185)
Fire Extinguishers	(220)
Pro Forma Adjustment	\$ 118

<sup>10</sup> Id., Adjustment C, Depreciation Expense.

g. Amortization. West McCracken proposes to increase its test-period operating expenses by \$875 to reflect amortizing rate case consulting fees of \$2,625 over three years.<sup>11</sup> Upon review of the supporting invoice from Kentucky Small Utility Consulting, Staff believes that the fee is reasonable and that the amortization should be reflected in West McCracken's pro forma operating expenses. Accordingly, Staff recommends the Commission accept West McCracken's proposed adjustment.

h. Payroll Taxes. West McCracken reports a test period payroll tax expense of \$13,209. Applying the current "FICA" rate of 7.65 percent to the \$7,371 decrease to salaries and wages – expense determined reasonable herein, Staff has determined that payroll tax expense should be decreased by \$564.<sup>12</sup> Accordingly, Staff recommends that payroll tax expense be decreased by that amount.

i. Loss from Disposition. In 2009, West McCracken disposed of an asset and recorded a loss of \$1,883, which it proposes to remove from its pro forma operations.<sup>13</sup> Because the loss on the disposition of the asset is a nonrecurring item that should not be reflected in pro forma operations, Staff agrees with West McCracken's proposed adjustment and recommends that the Commission accept West McCracken's adjustment to increase pro forma net operating income by \$1,883.

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<sup>11</sup> Id., Adjustment D, Amortization Expense.

<sup>12</sup> \$7,371 (Salaries and Wages – Employee Adjustment) x 7.65% (FICA Rate) = \$564.

<sup>13</sup> Application, Exhibit 4, Pro Forma, Reference Notes, Adjustment E, Loss from Disposition.

APPENDIX D  
STAFF REPORT, CASE NO. 2010-00454  
WEST MCCRACKEN'S  
REQUESTED WATER RATES

Minimum Bill with Zero Usage

5/8" Meter	\$	6.37
1" Meter	\$	15.92
2" Meter	\$	63.69
3" Meter	\$	95.51
4" Meter	\$	159.17

All Water Usage

First	100,000	Gallons	\$	5.10	Per 1,000 Gallons
Over	100,000	Gallons	\$	3.47	Per 1,000 Gallons

Bulk Water Sales

\$	5.50	Per 1,000 Gallons
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APPENDIX E  
STAFF REPORT, CASE NO. 2010-00454  
STAFF'S RATES WEST MCCRACKEN  
COULD JUSTIFY

Minimum Bill with Zero Usage

5/8" Meter	\$	7.74
1" Meter	\$	19.35
2" Meter	\$	77.38
3" Meter	\$	116.08
4" Meter	\$	193.46

All Water Usage

First	100,000	Gallons	\$	6.19	Per 1,000 Gallons
Over	100,000	Gallons	\$	4.21	Per 1,000 Gallons

Bulk Water Sales

\$	6.68	Per 1,000 Gallons
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William Tanner  
Superintendent  
West McCracken County Water District  
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West Paducah, KY 42086